In the Supreme Court
OF THE
United States

OCTOBER TERM, 1940

No.

JAMES H. JORDAN, J. R. MASON, L. F. ABADIE, GEORGE F. COVELL, and FIRST NATIONAL BANK OF TUSTIN (a corporation),
Petitioners,

vs.

PALO VERDE IRRIGATION DISTRICT, an irrigation district,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

STATEMENT OF THE CASE.

A concise statement of the case is contained in the foregoing petition under the heading of Summary Statement of the Matter Involved. Other facts are stated below. (pp. 27-35, 37-39.)

I. THE COURT WAS WITHOUT JURISDICTION TO ENTER THE DECREE.

It is respectfully suggested that the trial Court was wholly lacking in jurisdiction. The petitioner being exclusively governmental in nature seems to be entirely excluded by the terms of the act under which these proceedings were prosecuted.

In Section 83(c) of the Bankruptcy Act, which is Section 403, Title 11, U. S. C., after stating that the Court may enjoin proceedings and put the plan temporarily into effect, it is provided:

> "* * * but shall not, by any order or decree, in the proceeding or otherwise, interfere with (a) any of the political or governmental powers of the petitioner; * * *"

To make doubly sure that the political or governmental affairs of the State were not to be interfered with, Congress inserted in the Act subdivision (i) of the same section (83) which reads as follows:

> "(i) Nothing contained in this chapter shall be construed to limit or impair the power of any State to control, by legislation or otherwise, any municipality or any political subdivision of or in such State in the exercise of its political or governmental powers, including expenditures therefor."

Then further, to guard against the Act failing entirely because some petitioner might be a governmental agent Congress inserted:

> "* * * That if any provision of this chapter, or the application thereof to any such taxing agency or district or class thereof or to any circumstance,

> is held invalid, the remainder of the chapter, or the application of such provision to any other or different taxing agency or district or class thereof or to any other or different circumstances, shall not be affected by such holding." (Tit. 11, Sec. 401, U. S. C.)

In the case of *Luehrmann v. Drainage District No. 7*, 104 Fed. (2d) 696, the Circuit Court of Appeals seems to incline to our view that in *U. S. v. Bekins* the Court did not intend to hold the act to apply to an agency exclusively governmental. The Court there points out that the drainage district "is not a governmental agency" and the Court further points out the separability clause in the municipal bankruptcy act.

The decree in this case will limit the power of the district to levy taxes, will subject the district to all the terms of the R.F.C. Resolution, e. g., the district will not issue further bonds (R. 201, 213), will operate on cash basis (R. 213), will give R.F.C. notice of meetings (R. 215), submit annual reports (R. 216), exclude lands from the district. (R. 219.)

The decree in this case in effect says that the power of taxation is limited by the "ability" to pay of the taxpayer.

Furthermore, Section 10, Subd. 5 of the Palo Verde Irrigation District Act (Cal. Stats. 1923, Chapter 452) (see appendix p. viii) declares that property acquired by the district is vested

> "in trust for, and is hereby dedicated and set apart to, the uses and purposes set forth in this act."

In the case of *Anderson-Cottonwood Irrigation District v. Klukkert as assessor,* 13 Cal. (2d) 191, 88 Pac. (2d) 685, the district had taken over a considerable quantity of land through its assessment proceedings and the county assessed those lands for county tax purposes. The Court reviewed the authorities at some length and said:

> "Irrespective of that which hereinbefore has been stated with respect to the rule that under a constitutional provision exempting state-owned property from taxation it is immaterial whether the property is held in a proprietary or a governmental capacity, it does not appear that the lands here involved are nonoperative, within the meaning contended for by respondents. In the recent case entitled El Camino Irrigation District v. El Camino Land Corporation et al., Cal. Sup., 85 P. (2d) 123, this court held that an irrigation district was an agency of the state, whose functions were considered exclusively governmental; that it owns no lands in a proprietary sense, its property being owned by the state and held only for governmental purposes. The court pointed out that under section 29 of the Irrigation District Act, Deering's Gen. Laws 1931, Act 3854, pp. 1948, 1970, it was provided that property acquired by the district should be held 'in trust for', and was 'dedicated and set apart to the uses and purposes' set forth in the act. See, also, Clough v. Compton-Delevan Irrigation District et al. (12 Cal. (2d) 385) Cal. Sup., 85 P. (2d) 126; Moody v. Provident Irrigation District, Cal. Sup., 85 P. (2d) 128 (12 Cal. (2d) 389). Also, in the recent case entitled Provident Land Corporation v. Zumwalt et al., Cal. Sup., 85 P. (2d) 116 (12 Cal. (2d)

365), where the economic history of irrigation districts in this state was reviewed at some length, it was held that lands acquired by the district under the provisions of the Irrigation District Act remain in trust, and that their proceeds, whether by sale or lease, were likewise subject to the trust."

We contend that this district and this state property and this public trust can no more be subjected to the jurisdiction of the bankruptcy court than the State of California itself.

II. THERE IS ANOTHER ACTION PENDING IN THE STATE COURT.

The facts as recited show that at the time this proceeding was commenced there was an action pending under the irrigation district refinancing act. (Cal. Stats. 1937, p. 92.) Briefly this act provides that any irrigation district unable to pay its debts as they mature may initiate a proceeding for readjustment of its debts. The case is set down for hearing and if the Court finds that the plan is fair the district has the right to proceed to condemn the bonds that do not accept the plan. (Appendix p. ii.) That case had proceeded to the point where the judge ordered the interlocutory decree to be entered and then this bankruptcy proceeding was commenced and the district sought to dismiss its state Court proceeding. The effect of the pendency of those proceedings should be determined by this Court. Frankly, we urged the unconstitutionality of those proceedings in the Superior Court, but our contentions were overruled and un-

doubtedly the act is presumably constitutional. Such is the California rule. (*First National Bank v. South San Joaquin Irrigation District,* 9 Cal. (2d) 781, 72 Pac. (2d) 156.) But unless the act is declared unconstitutional, petitioners urge that that proceeding is a bar to the instant proceeding. There is no decision which determines this question and our position is that determination of this matter is requisite for the disposition of the instant case.

There is one very important section in that act which is also relevant to the question hereafter briefly discussed, namely the plan was executed fully out of Court. We refer to Section 19 from which we quote the following:

> "In the event that said petition for liquidation, refinancing or readjustment is dismissed, or that any of the provisions hereof for confirmation of the plan or acquisition of the bonds or warrants of the nonaccepting holders shall be declared invalid, such dismissal or declaration shall not affect the effectiveness of the plan with respect to the district or holders of bonds or warrants accepting the same."

It appears by this section that the Legislature intended that when the plan has been adopted and accepted by the requisite number, no matter what happened thereafter, the plan was in effect as to those creditors who had accepted the plan and as to the district.

We further refer to Section 5 of the Act which provides:

> "The Court in which said petition is filed shall have exclusive jurisdiction with respect to all

suits, actions and proceedings against the district" etc. (Appendix p. i.)

It is our position that this section gave to the Superior Court exclusive jurisdiction, and until those proceedings are terminated the district cannot confer jurisdiction upon the Federal Court by filing a petition there.

III. THE CAUSE IS RES JUDICATA.

As shown the district had a proceeding under the first municipal bankruptcy act which went to judgment. (R. 149, 295.)

The lower Court's opinion in the case of *West Coast Life Insurance Co. v. Merced Irrigation District,* 114 Fed. (2d) 654, seems to take the position that no reasons were given by the Circuit Court of Appeals in the first municipal bankruptcy case there discussed, and that the decision is not *res judicata* of any question whatever.

Under the authority of the important cases of *Chicot County Drainage District v. Baxter State Bank,* 308 U. S. 371, and *Stoll v. Gottlieb,* 305 U. S. 165, it must be considered that the Court had jurisdiction to enter its judgment and thereby to determine all issues. Among these issues is the issue of unconstitutionality. This issue is precisely set forth in the record at R. 298. At this same page in the record it is shown that the first bankruptcy case came on for trial and was heard by the Court and tried on the merits, and on December 8, 1936 Judge Cosgrave entered a judgment of dismissal. It seems to us that if the

Court, under a supposedly unconstitutional statute, can as in the *Baxter State Bank* case, supra, make a binding decree that the plan is constitutional and valid as between the parties, that the Court can, under such a statute, enter a decree that the plan is unconstitutional and invalid as between the parties. This is the situation here.

We refer to the general rule that

> "The legislature may not, under the guise of an act affecting remedies, annul, set aside, or impair final judgments obtained before the passage of the act."
>
> 12 *C. J.* 984;
>
> *McCullough v. Virginia,* 172 U. S. 102.

> "The policy of the law or constitutional principle involved very clearly is that rights of property, once vested * * * by judicial decision then finally between the parties shall not afterwards be disturbed or the controversy opened by mere legislative enactment."
>
> *Lancaster v. Barr,* 25 Wis. 560, 562.

In California a judgment is a contract. *Scarborough v. Dugan,* 10 Cal. 305. In *Frost v. City of Los Angeles,* 181 Cal. 22, the Supreme Court of California said, in pointing out that an amendment of an unconstitutional statute making it constitutional does not have a retroactive effect:

> "* * * the answer is that amendments to the law do not operate upon an existing suit in a case like the present, nor have retroactive effect so as to affect the validity of a judgment rendered before the new law came into existence."

IV. THE R.F.C. IS NOT A CREDITOR AFFECTED BY THE PLAN.

The statute requires that the petition must allege that 51 per centum in amount of securities affected by the plan, excluding those owned, held or controlled by the petitioner had accepted it. The statute also requires that two-thirds of the actual amount of the claims affected by the plan must accept it before the plan is confirmed. In subdivision (a) of Section 82 it is provided that "no creditor shall be deemed to be affected by any plan of composition unless the same shall affect his interest materially . . ." and Section 82 provides that the terms "security affected by the plan" means security as to which the rights of the holder are to be adjusted or modified materially.

Now prior to March 1, 1934, the district applied to the R.F.C. for a loan and a loan was approved on March 1, 1934. (R. 201, 223.) The plan set up by this resolution has never been changed or modified and an election authorizing the loan (to be secured by new bonds) was held on June 15, 1934. (R. 223.) An agreement was made between the district and the R.F.C. August 7, 1934 (R. 225) and on the same date a second agreement (R. 236) was made. It was stipulated, however, that the first agreement was made before the second agreement was made. (R. 225.) Disbursement by the R.F.C. was on October 31, 1934 (R. 224) at which time the R.F.C. acquired possession of 96.76 per cent of the old bonds. (R. 224.)

On March 1, 1934 when the loan was approved there was no bankruptcy statute on this subject. The R.F.C. resolution at R. 204 states that no loan shall be made

unless all the old securities are deposited, or the R.F.C. is satisfied that a sufficiently large proportion has been deposited. Since more than 90 per cent had been deposited and the corporation actually disbursed on October 31, 1934, it seems that the Division Chief was satisfied. Subdivision (b) of Section 5 of this resolution (R. 208) provides that if the Division Chief deems it necessary to keep any of the deposited securities alive in order to maintain a "parity" of rights the loan may be made directly to owners' agents or to consenting owners, but this was not done. If the matter was to be handled by a note given by owners' agents then a note would be executed and secured with a pledge of the securities. But that was not done.

The first agreement (R. 225) seems to be entirely in accordance with the resolution of March 1, 1934. In the second agreement (R. 236) we find the proposition put forward for the first time, that the loan may be made by the R.F.C. acquiring the old securities. This does not seem to be authorized by the election the people voted on (R. 223), which was for an issue of new bonds to secure the loan, especially when we consider that the district paid considerable sums of public money for the purpose of bringing about the refinancing, which it could not do if it was merely transferring ownership from one security holder to another. Unless in fact the transaction at the time it was concluded, had the effect of then reducing the debt it was ultra vires both as to the California Statutes 1917, p. 243, and Title 43 Section 403, U. S. C.

Section 3 of California Statutes 1917, p. 243, as amended, provides that such contract must be approved at an election.

Title 43 Section 403 U. S. C. provides that no loan may be made by the R.F.C. until satisfied that a substantial reduction will be effected in the debt of the district.

The California Statute referred to does not authorize a contract for purchase of the district's old bonds.

The Federal Statute does not authorize the R.F.C., we contend, to advance any money on its loan unless such advance automatically reduces the district's debt.

Where the rights of third parties have attached the conduct of the parties is a relevant part of the transaction.

1 *Mechem, Sales,* 1901, Sec. 46, page 45.
Insurance Co. v. Dutcher, 95 U. S. 269, 273;
Topliff v. Topliff, 122 U. S. 121, 131;
District of Columbia v. Gallaher, 124 U. S. 505, 510.

Furthermore Title 15, Section 604a U. S. C. provides that a loan by the R.F.C. expires in a year and therefore the R.F.C. could not make any further disbursements out of the loan, part of which was disbursed in October, 1934. As everything had to be done within that year, the plan could not remain open.

Order No. 8 of the Districts Securities Commission (R. 278), which is the comission having fiscal supervision of the district, provides in paragraph 3 "that said refunding bonds be issued to repay the Recon-

struction Finance Corporation for equal amounts of loans provided by said corporation . . .". The second rehabilitation plan (R. 272) says that a charge will be collected to cover "interest and principal on R.F.C. loan". The same reference is found in the third rehabilitation plan. A letter from the district to the bondholders dated April 16, 1934 (R. 242) contains this statement:

> "As a result of negotiations with representatives of all groups of bondholders the district is now in a position to make the following cash offer for your bonds:"

The bondholders in their escrow agreement stated (R. 172):

> "I hand you herewith.....bonds....., which you are authorized to deliver to or upon the order of the Board of Trustees of said Palo Verde Irrigation District. . . ."

Another important link in the chain is the resolution authorizing instructions to the Security First National Bank (Respondent's Exhibit A (R. 178):

> "For the purpose of consummating the loan for which Palo Verde Irrigation District heretofore applied * * * deliver * * * for the account of the Reconstruction Finance Corporation upon collection * * * for the account of this District, of a sum equal to $1000 plus 24.81¢ per dollar of the aggregate principal amount of said bonds" (R. 179),

and then specifically instructed

> "From the proceeds received from the Federal Reserve Bank pay $1000.00 * * * also pay to Palo

> Verde Properties, Inc. * * * $5.00 for each $1000.00 of principal * * * also pay to yourselves the sum of * * * $500.00."

These instructions also provided for contributions by the district of $1158.08 towards the expense of the escrow. (R. 180.)

This resolution was adopted October 26, 1934, and it was headed "Resolution Authorizing Instructions * * * in the matter of closing Reconstruction Finance Corporation Loan Escrow."

The money advanced was paid to the district.

Now if this was an outright purchase of bonds by the R.F.C. and if that was the intention of the bondholders when they deposited their bonds in escrow and of the R.F.C. in depositing the amount of the loan with the Federal Reserve Bank and of the district, why was it necessary for the district thus to participate in the escrow? The answer is obvious. It was because the bondholders considered that they were surrendering their bonds to the district pursuant to the letter from the district that the district was now able to pay cash and to make a certain cash offer for the bonds, whereby the bonds would be paid off and cancelled, and they were therefore appropriately delivering the bonds to the district or its order.

Lastly, attention is called to the fact that the district paid some $1400.00 or $1500.00 in the transaction. (R. 177, 180.) The payment of that sum by the district fits in very well with the theory of the petitioners, that the R.F.C. made a loan to the district

and that its only right is to receive refunding bonds. It is our position that this transaction constituted a pledge securing a loan made direct to the district. (*In re Grand Union Co.,* 219 Fed. 353, 359, certiorari denied 238 U. S. 626 and appeal dismissed 238 U. S. 647; *In re Rogers,* 20 Fed. Sup. 120, 129; *Jones v. Third National Bank of Sedalia,* 13 Fed. (2d) 86; *Shelley v. Byers,* 73 Cal. App. 44.)

The transaction is to be judged by California law. (R. 225, 234.)

Furthermore the R.F.C. (R. 150, 328) filed a written consent to the plan of composition in the state Court proceedings under California Statutes, 1937, Ch. 24.

Sec. 19 enacts that where such a consent is filed the plan becomes binding on the creditor. (Appendix p. ii.)

If the bonds are held as security by the R.F.C., for a loan granted the district, then the district must be the beneficial owner of the bonds. The R.F.C. could not possibly collect more from the district on those bonds than it advanced on the loan, with interest at 4 per cent. After that has been paid, the obligation represented by those bonds would be paid. Therefore the district is the beneficial owner. Except for the effect of Section 82 which provides: "any agency of the United States holding securities acquired pursuant to contract with any petitioner under this chapter shall be deemed a creditor in the amount of the full face value thereof." and of 83 (j) providing that "the partial completion or execution of any plan of composition . . . by the exchange of new evidences of indebtedness under the plan for evidences of indebted-

ness covered by the plan, . . . shall not be construed as limiting or prohibiting the effect of this title, and the written consent of the holders of any securities outstanding as the result of any such partial completion . . . shall be included as consenting creditors to such plan of composition in determining the percentage of securities affected by such plan of composition.", and except for the proposition that a governmental agency is to have its contract judged by different rules than citizens, there would seem to be no question but that the vote of the R.F.C. could not be counted in the necessary percentage.

We point out that Congress in Section 82 did not say that the R.F.C., though deemed a creditor in the amount of the full face value of the securities acquired, is to be deemed to be adversely affected by the plan of composition, nor did Congress say in Subdivision (j) of Section 83 that in a case where securities had not been exchanged the consent of the parties could be counted in determining the percentage.

We further point out that the committee on the judiciary in its report No. 1901 dated March 29, 1940, to the 76th Congress, Third Session, referring to HR9139, a bill for the amendment of Sections 81 and 83 of the Bankruptcy Act, rejected a proposed amendment to the Bankruptcy Act which would provide that acceptance of refunding bonds under a refunding plan would, of itself, constitute acceptance of the plan in bankruptcy. The committee said:

> "Your committee are of the opinion that the time element is important in this connection, and that regardless of the terms and conditions of the plan

> previously accepted by the bondholder, and even regardless of whether the plan in bankruptcy is not less favorable than the refunding plan previously accepted by the bondholder, the law should permit the bondholder to have the opportunity of accepting or rejecting the plan in bankruptcy at the time such plan is submitted to the bondholder."

Much more along the same line is said in this committee report. The point is that it indicates very strongly that Congress intended that the question of consent should have vital importance as a jurisdictional requirement. There must be consent by present creditors who must have the opportunity to say whether or not they do consent under the conditions existing at the time the bankruptcy petition is filed. Now the original Palo Verde bondholders have gone their way, it is not possible to obtain their consent. We contend that it is inequitable to permit the R.F.C. to consent for them especially where they paid only 25¢ on the dollar for those securities. The R.F.C. cannot express the independent judgment of the investing public. The R.F.C. will be beneficially affected and not adversely affected. The R.F.C. is nothing but the fiscal agent of the district. It expresses every wish and desire of the district and from the very beginning worked hand in hand with the district to secure the desired reduction of indebtedness. All that is said by this Court in *American United Mutual Life Insurance Company v. City of Avon Park,* ..... U. S. ....., 61 S. Ct. 157, on the question of consent is pertinent here, and unless this public agency should have its con-

tract weighed by different scales than the rules of law which apply to the contracts of private individuals, but one conclusion, we submit, can be reached, and that is that the consent is ineffective. We do not believe that Congress has gone so far as to say that where the R.F.C. is a party the ordinary principles of equity are not to be applied in a bankruptcy proceeding.

V. THE PLAN IS ONE FULLY EXECUTED OUT OF COURT AND NOT PURSUANT TO THE STATUTE.

In the case of *In re West Palm Beach,* 96 Fed. (2d) 85, the Court held that a plan which has been partially executed is incapable of presentation as a composition. In that case the plan has been carried out by the exchange of securities. Congress thereafter enacted subdivision (j), Section 83, providing that the partial completion of a plan of composition "by the exchange of new evidences of indebtedness" could not be construed as limiting or prohibiting the "effect of this title" and that such written consent should be included.

Petitioners question the power of Congress to pass such a statute, particularly where the statute still requires that the persons consenting shall be adversely affected in order to execute a valid consent.

We also contend that the doctrine of *inclusio unius exclusio alterius* results in the conclusion that where the loan has been made but actual securities have not been exchanged rules of equity will still apply.

If the R.F.C. is regarded as a holder of original bonds then the plan was fully effected when the first bankruptcy petition was filed and adjudicated. If this is not conclusive, then Section 19 of California Statutes, 1937, Ch. 24 (Appendix, p. ii) which provides that the effectiveness of the plan cannot be affected by the dismissal of the proceedings comes into force.

VI. THE CLAIMS ARE NOT ALL OF THE SAME CLASS.

Some of the petitioners hold an alternative writ of mandate which is still in force in the State Court requiring the payment of their matured bonds and coupons and tying up of the funds of the district. (R. 303-7.) This writ of mandate is a vested right. (*Borough of Ft. Lee v. U. S.*, 104 Fed. (2d) 275.) Furthermore, some of the petitioners are holders of judgments in the State Court and these judgments are not only against the district, but they are also against the drainage district and the levee district. (R. 315, 318.) Appeals were taken from these judgments and the appeals have not been concluded. Prima facie, these judgments are valid.

VII. THE PLAN OF COMPOSITION IS NOT FAIR, EQUITABLE, OR FOR THE BEST INTEREST OF CREDITORS AND IT IS DISCRIMINATORY.

In the first place the district is not insolvent and the rule in *Case v. Los Angeles Lumber Products Co.*, 308 U. S. 106, seems to require that the minimum the

plan should offer is a vastly more generous payment to the bondholders.

The bond debt of the district as disclosed by the petition was $4,174,330.36 plus a note of $4000.00. (R. 22.)

The amount of the R.F.C. loan was $1,039,423.00. (R. 13.)

The R.F.C. appears to hold in substance all the bonds except petitioners'. The holdings of the petitioners at the time of the hearing was $79,000.00.[1] (R. 58, 59.)

The assessed value of the land in the district was more than $5,000,000.00 in 1927 and approximately $3,000,000.00 in 1937. (R. 258.) The appraiser for the R.F.C. loan placed a value on the lands of $70.00 to $80.00 per acre, speaking of clear and improved land. (R. 295.) This for 30,000 acres of land which is the minimum of good land in the district, would be two and a quarter million dollars, or more than twice the amount offered the bondholders. In view of the fact that the district owned over 99 per cent of this land, the justice of the payment of twenty-five cents on the dollar is not apparent.

Second, the holders of the private mortgage bonds (Mutual Water Company) received fifty cents on the dollar of principal for their bonds, but the public bondholders receive less than 25%. (R. 180, 181.) The

1. Irrigation District Bonds $38,000.00.
Levee District Bonds $32,000.00.
Drainage District Bonds $9000.00.
Covell surrendered his $10,000.00 Irrigation District bonds but holds the coupons. Jordan owns a block of coupons from bonds already deposited.

plan proposed 24.81¢ per dollar of principal (R. 22), and the district by resolution directed the bank to "deliver" the deposited bonds "for the account of the Reconstruction Finance Corporation" upon "collection" of 24.81¢ per dollar (R. 179) but directed the bank out of this "collection" to disburse 50¢ on the dollar to the holders of Mutual Water Company bonds and 23.248¢ to the public bondholders. (R. 180.) The trust officer handling the transaction also verified this. (R. 181.) In point of law the public bondholders have a superior claim. There is no evidence before the Court anywhere justifying such discrimination. This discrimination would seemingly invalidate the plan. (*American United Mutual Life Insurance Company v. City of Avon Park,* ..... U. S. ....., 61 S. Ct. 157.)

Further, it is unjust if not unconstitutional that the state should be enriched. This district owns over 99 per cent of the land. (R. 197, 264.) It may not thus confiscate private property and public bonds to pay a public debt. (Article XI, Sec. 15, California Constitution.)

It is unfair to pay the bondholder only such amount as a bank (the R.F.C.) is willing to loan. These creditors are willing to loan more. They wish merely to keep their bonds.

Section 4 of California Statutes, 1931, p. 2263, prohibits the issue of the proposed bonds to the R.F.C. except upon a finding by the Districts Securities Commission that they do not exceed 60 per cent of the value of the bare lands plus the works of the district.

Is it not conclusive that the plan does not offer more than 60 per cent of the value of the assets?

The loan of the R.F.C. is for 33 years only. These bonds could have been issued for 50 years. Even 10 years added to the bond issue would have materially increased the amount to be paid the bondholders.

The R.F.C. as a creditor will receive 4 per cent and does receive 4 per cent interest on its claims and will receive in exchange for its claims a bond bearing 4 per cent which is tax exempt. These creditors must take cash and find a new investment.

The trust funds of the district amounting to $100,000 in cash (R. 274) already earmarked by a writ of mandate (R. 304) are taken from petitioners. *Provident Land Corp. v. Zumwalt,* 12 Cal. (2d) 365, 85 Pac. (2d) 116. Likewise other trust properties of the district, being all of the assets and properties on hand are taken from petitioners.

It is unfair to scale down the claims of these creditors when other bond issues of the county and the City of Blythe are not similarly scaled down. (R. 193.) County bonds have been paid 100¢. (R. 314.) Such bonds are not superior in point of law to petitioners' bonds. In fact, under the decision in the case of *Anderson-Cottonwood Irrigation District v. Klukkert,* 13 Cal. (2d) 191, 88 Pac. (2d) 685, this district now owns all the land in the district free of right of the county to levy taxes upon it and these county bonds could only be collected if, as and when these lands go back on the tax roll and pass out of the hands of the irrigation district. Thus the irrigation

district could operate these lands under leases and provide a much greater payment for the benefit of the bondholders. Yet the plan of composition is in no way based upon the value of the water rights, canals and lands.

The petitioners, who are holders of levee bonds, have a right to an assessment against the personal property as well as the real property of the landowners and this right was in no way taken into consideration. (1905 Cal. Stats. Ch. 310, Sec. 10.) (Appendix p. v.)

VIII. THE PLAN OF COMPOSITION IS NOT PRESENTED IN GOOD FAITH.

The hearing in this case lasted approximately an hour and a half and the evidence consisted of the transcript of proceedings taken in a former hearing in the state Superior Court. The S.E.C. does not intervene in these proceedings. The trial of such a cause is not a proceeding between two adverse parties, but one in which the Court itself should take an active hand.

First National Bank v. Florsheim, 290 U. S. 504, 525;

National Surety Co. v. Coriell, 289 U. S. 426, 436.

A long list of harassments by the district include injunctions against the prosecution of these petitioners' rights in the State Court. These injunctions have been outstandingly effective since 1935.

The execution of the second agreement, Exhibit 20 (R. 236) amounts to connivance by the R.F.C. to establish ownership by that agency of the bonds. There is an old saying that what everyone knows must be true, and in this case everyone knows that this district has already been refinanced. The fiction is maintained by the conduct of these parties through such documents as Exhibit 20.

Lastly the district contributed approximately $1450 to the purchase of the bonds by the R.F.C. (R. 170, 180-181.) Thus these bonds are in some sense within the control of the district. The fact that the escrow agreement showed that the bondholders surrendered them to the order of the district, shows that that control is a real thing.

Much we have said supra under IV the R.F.C. is Not a Creditor Affected by the Plan, applies here.

IX. THE STATE AS A DEBTOR CANNOT REPUDIATE ITS OBLIGATIONS.

Since the district actually owns title to 99.66 per cent of the real estate and the state issued these bonds subject to the limited right to collect them from the state out of assessments on properties in this district, the state in this case would appear as the owner of the property to be in a peculiar sense the debtor of the bonds. The State of California owning the bonds and assets including its valuable water rights on the Colorado River (R. 186) coming into Court to destroy this public trust which is established by its own

statutes, seems to run counter to any concept of equity. These bonds bear the seal of the state and the certificate of the state controller irrevocably certifying them as lawful investments for savings banks, trust funds and the like. (See Appendix p. xvi.) There is certainly room for argument that within the meaning of the constitution the bankruptcy concept does not embrace the state. (Minority opinion by Mr. Justice Cardozo in *Ashton v. Cameron County Water Improvement District No. 1,* 298 U. S. 513, 56 S. Ct. 892.)

X. THE DECREE UNLAWFULLY TAKES TRUST FUNDS AND VESTED RIGHTS.

Appellant Jordan has a judgment against the Palo Verde Drainage District, the Palo Verde Joint Levee District of Riverside and Imperial Counties, California. (R. 300, 315, 318.) First Bank of Tustin likewise has a judgment against the drainage district. These judgments are not final because appeals were taken. They are judgments and contracts. The judgment is property and a vested right. They are judgments against other debtors than the bankrupt. Release of one party to the liability does not necessarily release the others.

Each of the petitioners has a vested right in the writ of mandate which impounded certain funds.

That the assessments are trust properties has long been the law of California. (*LaForge v. Magee,* 6 Cal. 650, 651; *People v. Bond,* 10 Cal. 563 at 573,

574.) Section 29 of the Palo Verde Irrigation District Act as amended in 1927, California Statutes, 1927, page 972, at 997, reads as follows:

> "All moneys collected from the district, either from taxes or from any other source, shall be paid by the collector to the county treasurer of the county of Riverside and placed in a fund to be called 'Palo Verde irrigation district fund.' It shall be the duty of said county treasurer, upon presentation of any matured bond or interest coupon of any bond of any of said three districts, to pay the same from said fund."

Section 10, Subd. 5 of the Palo Verde Irrigation District Act provides as follows:

> "The legal title to all property acquired under the provisions of this act shall immediately, by operation of law, vest in the district, and shall be held by the district in trust for, and is hereby dedicated and set apart to, the uses and purposes set forth in this act. And said board is hereby authorized and directed to hold, use, manage, keep and possess, said property as herein provided." (Appendix p. viii.)

This is substantially the same provision as Section 29 of the California Irrigation District Act which was interpreted by the Supreme Court in a number of cases, particularly in the case of *Provident Land Corp. v. Zumwalt,* 12 Cal. (2d) 365, 85 Pac. (2d) 116, where the Court said:

> "the lands remain in trust, and the district exercises its powers, however broad, as a trustee. Once it is made clear that the lands are held in

trust, it necessarily follows that their proceeds, whether by sale or lease, are likewise subject to the trust. It would be manifestly absurd to say that although property is held in trust, none of the benefits of the trust accrue to the beneficiaries, and that none of the rents or profits of the trust property need be used in furtherance of the trust purposes. On this point, namely, that the land is trust property, held for the 'uses and purposses' of the act, and that the proceeds are stamped with the character of the property from which they flow, the statute, read in the light of elementary principles, leaves no room for debate."

"It next becomes necessary to determine whether payment of the bondholders is one of these purposes. * * * defendants and amici curiae vigorously contend that * * * creation of debts is not one of its purposes. * * * This type of argument, however, tends to prove too much * * * But laying aside quibbles as to the exact meaning of the phrase 'uses and purposes', it seems clear that if the district is to be created and to function on borrowed money, repayment of the money is not a wholly immaterial and foreign objective. Evading creditors is not a contemplated activity of a public district, whose bonds are recognized investments for financial institutions. Among other purposes of the act, therefore, is the repayment of the bondholders of the district, and it follows that this is one of the purposes for which the trust money is held."

"The land is the ultimate and only source of payment of the bonds. It can never be permanently released from the obligation of the bonds until they are paid * * * Any practice which removes the land from its position as ultimate

> security for the bonds, or which places its proceeds beyond the reach of the bondholders, destroys that plan and is contrary to the spirit of the act."

Thus all the lands, cash and other assets of the district are trust properties right to which is vested in petitioner.

XI. THE LIABILITY OF THE LEVEE DISTRICT AND OF THE DRAINAGE DISTRICT AND OF THE COUNTY OF RIVERSIDE WAS NOT TAKEN INTO CONSIDERATION BY THE COURT.

We present the sole proposition here that Section 12 and 13 of the Palo Verde Irrigation District Act (Appendix pp. ix, xiii) preserved the existence of these districts in order to preserve their liability and a bankruptcy decree which terminates the liability of the Palo Verde Irrigation District does not terminate the liability of these other agencies.

XII. THE LOWER COURT ERRED IN HOLDING THAT CERTAIN POINTS WERE NOT PRESENTED TO THE TRIAL COURT.

Chapter IX of the Bankruptcy Act provides that any creditor may file an answer. Section 83 (b). The section goes on to provide that the Court may not confirm the plan unless the Court is satisfied that the plan is fair, that it complies with the provisions of the chapter and is properly accepted, the amounts paid by petitioner are reasonable, the plan is in good faith, and so forth. It would appear therefore that any creditor could appeal if the decision did not properly establish these essentials.

However, the petitioners did raise each and every one of their points in their answer (R. 57) and the case was tried in the Superior Court on similar objections and the record is full of objections made to the introduction of testimony, motions, stipulations and vidence bearing out that the case was tried on the theory of the objections raised. The narrative statement of evidence shows (R. 147) that the cause came on for hearing upon the petition and the answer and objections of the respondents. The minute order of the Court (R. 91) shows that the objections filed by the appellants were overruled. Since the three oral objections made to the introduction of testimony at the opening of the hearing were not written objections, they were not filed, and the Court must have referred to the other objections. The stipulation of the parties (R. 46) shows that the transcript of evidence was introduced with the objections and rulings thereon. An example of an objection to the testimony is shown at R. 265. A written stipulation (R. 295 to 307) covered evidence on many points which have been urged by petitioners. This Court below stated that propositions 4 and 6 to 13 were not urged in the trial Court. (114 Fed. (2d) at 694.) Categorically proposition 4 was presented by the answer. (R. 60-62.) Proposition 6 by the answer. (R. 63.) Proposition 7, the answer twice denies the plan is fair. (R. 61-64.) Proposition 11 is covered at R. 66. Proposition 13 is specifically alleged in the answer. (R. 67.) Several of the points were again called to the trial court's attention in our objections to the Findings. (R. 124.)

CONCLUSION.

It is submitted that a writ of certiorari should be granted, the decree of the Court below reversed and the proceeding directed to be dismissed.

Dated, Turlock, California,
January 6, 1941.

Respectfully submitted,
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Counsel for Petitioners.

(Appendix Follows.)